

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

RECEIVED
SEP 22 11 49 AM '00
OFFICE OF THE CLERK
U.S. DEPARTMENT OF JUSTICE

POSTAL RATE AND FEE CHANGES, 2000

Docket No. R2000-1

REPLY BRIEF OF THE
ALLIANCE OF INDEPENDENT STORE OWNERS AND PROFESSIONALS

Communications with respect to this document may be sent to:

Donna E. Hanbery, Esq.
Executive Director
Alliance of Independent Store Owners
and Professionals
3725 Multifoods Tower
Minneapolis, MN 55402

September 22, 2000

TABLE OF CONTENTS

<u>Section</u>	<u>Page</u>
Summary of Reply Brief	1
NAA/AAPS Argument—One Plus One Equals (b)(4)	2
The (b)(4) Bluff	11
Conclusion	13

SUMMARY OF REPLY BRIEF

The Alliance of Independent Store Owners and Professionals (AISOP) submitted an Initial Brief requesting (1) that the Commission recommend rates for Standard A ECR saturation mail that are no higher than the rates proposed by the USPS, (2) that any savings in the revenue requirement be applied in part to reduce the proposed rates for Standard A ECR letter mail, and (3) supporting a reduction in the ECR pound rate.

AISOP's Initial Brief explained why affordable saturation mail helps small business advertisers and consumers and gave market information about the price sensitivity of this mail. It showed how a reduction in the pound rate will help mailers, advertisers, consumers, and the USPS. AISOP's Initial Brief examines the proposals made by the Newspaper Association of America (NAA) and the Association of Alternate Postal Systems (AAPS) to increase ECR cost coverages, and in turn postal rates, and to maintain or increase the pound rate and shows that there is no evidence on the record that the USPS ECR proposals will hurt the newspaper or alternate delivery industry. Instead, the record shows that Criterion (b)(4) of the Postal Reorganization Act (the Act) would favor the USPS ECR proposals as benefitting the general public, mailers, and small business advertisers who do not have other cost-effective alternatives to deliver their advertising to consumers.

The purpose of this Reply Brief is limited to showing that some of the factual statements, or implications, made in the Initial Briefs of AAPS and NAA are not supported by the record. In many cases, the arguments made by AAPS and NAA only tell part of the story. This Reply Brief will discuss some of the arguments made and provide references to record evidence that tells the rest of the story.

NAA/AAPS ARGUMENT—ONE PLUS ONE EQUALS (b)(4)

If the AAPS/NAA argument in support of higher rates for Standard A ECR mail was reduced to a simple theorem or proof, it would look something like this:

1. NAA and AAPS both oppose the USPS proposals for Standard A ECR mail under Criterion (b)(4) of the Act and allege, “The alternate delivery industry would suffer significant harm from a reduction in the pound rate.” (NAA Initial Brief at p.7.)

2. As evidence of “harm,” both NAA and AAPS rely solely on the testimony of Witness White. (TR14848; TR14895.)

3. The only factual evidence of “harm” White or NAA provide with respect to postal rates is to describe alternate delivery’s alleged loss of magazine business resulting from the Commission’s decision regarding the reclassification of periodicals in 1995. (AAPS-T-1 at p.13; TR19141-19142.)

4. The USPS’s former Postmaster General, Marvin Runyon, had the bad taste to state publicly at a Postmaster’s Leadership Conference that he was pleased that Publishers Express, the alternate delivery company delivering magazines, had gone out of business because the USPS had improved service and lowered its costs. (AAPS-T-1 at p.15.)

5. If the USPS was happy to see a competitive business close in the past, it follows that the USPS must have an evil motive with respect to any proposals concerning mail for which it competes today. (AAPS-T-1 at p.14.)

6. The Commission should take it on faith that when NAA and AAPS say proposed USPS rates “will harm” them that this must be true because postal rates hurt alternate delivery once before. NAA plus AAPS equals (b)(4).

NAA’s Initial Brief suggests that the Commission has not given ample credence to the postal fears of the alternate delivery industry in the past. NAA’s Initial Brief states, “In Docket No.

MC95-1, the alternate delivery industry testified that the proposed reclassification of second-class mail would cause great harm to their businesses. Bitter experiences prove them correct. The Commission should not allow the Postal Service to gloat in the future about the demise of yet another form of private competition.” (NAA Initial Brief at p.9.)

This is not an accurate representation of the record in this case or in Docket No. MC95-1. There is no record evidence in this case that the alternate delivery industry, or AAPS, opposed the reclassification of periodicals or is seeking higher rates for periodicals today. (USPS/AAPS-T1-10.) AAPS, and its longstanding torch bearer Witness Bradstreet, did not submit testimony that “the proposed reclassification of second-class mail would cause great harm to their businesses” as asserted in NAA’s Initial Brief. The Commission’s decision in Docket No. MC95-1 does not list AAPS as one of the opponents of the reclassification proposal for periodicals. (PRC Op. MC95-1 at V-83 to V-92.) AAPS in Docket No. MC95-1, as in this docket, and all other rate cases in which it, or its predecessor, the Coalition of Nonpostal Media submitted testimony, confined its testimony to urging the Commission to adopt the highest rates possible for saturation mail.

The testimony about alternate delivery’s experience with periodicals is a red herring. Neither AAPS nor NAA fought periodical reclassification on the grounds that it would “cause great harm” to the alternate delivery business. The only reason this issue is being raised now is to be able to point to a former Postmaster General’s “gloating” over the recapture of periodical business and to divert the Commission from focusing on the total lack of evidence showing actual or potential harm that NAA’s or AAPS’s members would suffer from the USPS’s ECR proposals.

Here are some additional examples where the arguments of AAPS and NAA only tell part of the story, or are completely rebutted by the record before the Commission.

AAPS asserts that the Commission’s approval of the USPS’s ECR proposals would “wipe out the only effective competition for the USPS in much of the advertising delivery market.” (AAPS

Initial Brief at p.2.) To borrow a phrase of NAA counsel in discrediting Witness Haldi, this assertion “does not pass the laugh test.” There is abundant evidence before this Commission on the record, and inserted in each Sunday’s *Washington Post*, that the USPS faces very effective competition from the newspaper industry in the delivery of advertising. (USPS-RT-19, see attached exhibits of newspaper advertising expenditures; PostCom-RT-1 at p.2 (Witness Harding states, “Let me begin by stating that over 90% of the print media we place is with newspapers.”).)

AAPS asserts in its Initial Brief that, “Mr. White testified that the pound rate reduction would permit the mailing of shared mail packages at prices that are lower than alternate delivery costs.” (TR9940.) The resulting loss of volume, he testified, would have the effect of “forcing alternate delivery companies out of business.” (AAPS Initial Brief at p.2.) A simple comparison of the rates charged by Mr. White’s company, DSO, and the proposed USPS rates, rebuts this contention. DSO’s publishes saturation rates for a five ounce piece vary from 7.3 cents to 13.8 cents each. Lower, off the rate card rates are available by negotiation with advertisers committing to large frequency and circulation but these were not revealed on the record. Even at the highest rates DSO charges, which presumably are rates higher than its “costs,” its rates are more attractive than the 16.86 cents rate that a mailer, entering a five ounce piece at the DDU, would pay under the USPS’s ECR proposal. For the high volume DSO advertiser, DSO’s published rates still are approximately half of the USPS’s proposed rates.

Both NAA and AAPS cite Witness Wilson as authority for their assertion that the USPS proposal could be the “death knell of the alternate delivery industry.” (TR19136; AAPS Initial Brief at p.2; NAA Initial Brief at pps.10 and 11.) Witness Wilson does not work for the “alternate delivery industry.” He handles distribution and special projects for Knight Ridder newspapers. There is absolutely no evidence that Knight Ridder is “on the ropes.” It was ranked by *Advertising Age* as number 14 of the 100 leading media companies for 1998 (NAA/AISOP-T2-1) and has operating

profit margins of 19.3% (TR19178). Knight Ridder has been able to make a tidy profit and keep its customers happy by using the USPS to deliver its TMC programs to nonsubscribers. Knight Ridder will not shut down its operations if the Commission approves the USPS's ECR proposals. It may consider shifting additional volumes from its private delivery distributions to postal delivery. But AISOP submits this is not a bad thing. Why should the Commission be implored to set artificially high rates for saturation mail to help newspaper companies keep more of their TMC distribution in alternate delivery? This does not help the general public and other mailers. It certainly does not help AISOP's small business retailers, service providers, professionals, tradespersons, and home-based businesses who do not have affordable alternatives to saturation shared mail programs to reach their customers.¹ It doesn't really even help newspapers compete. High postal rates allow newspaper companies to charge advertisers artificially high (not cost-based) rates for insert or preprint advertising because the only other alternative (postal delivery) costs so much more.

Even NAA Witness Wilson admitted that the high density ECR rates and service available to newspapers with TMC programs were favorable.²

¹Under Criterion (b)(5) of the Act, the Commission is to consider "the available alternative means of sending and receiving letters and other mail matter at reasonable costs." (§3622(b)(5).) As discussed in AISOP's Initial Brief, the record shows that saturation mailers, that include free papers, shoppers, coupon envelope mailers, and other shared mailers, offer small buys (generally 10,000 to 15,000 homes) of geographically targeted saturation mail advertising that lets small business only pay to reach customers in their market area. There is no reasonably priced alternative means of advertising for many small businesses. The Neighborhood, a zoned program offered by Witness Wilson's *Miami Herald* would charge an advertiser more than four times the cost for a like size ad in the mailed shopper, *The Flyer*, to reach only 20% to 25% of the occupied households in the small business's market area. In other words, daily newspapers do not choose to focus on small business customers. They charge them too much, to cover too wide an area, and reach too few people.

²If anything, the USPS proposed ECR rates are more favorable to the competitive position of newspaper TMCs than they are to saturation mailers. The proposed increase for ECR saturation mail varies from 5.3% to 5.9%. The proposed increases for ECR high density mail (used by newspaper TMCs) are .8% to 1.5%. The pound rate reduction that would apply to saturation and ECR high density mail is the same. The record shows that the costs of delivery for selective delivery

Q. Would it be fair to say that in your choices of creating a nonsubscriber program to distribute by mail or some form of alternate delivery, that one of the things you look at is your postal costs in doing this by mail?

A. Yes, ma'am.

Q. And if postal rates were to increase, would you be doing a cost-benefit evaluation of whether staying in the mail or converting more or all of your circulation to private carrier would be the best option for you?

A. Since the postal rates are our benchmark, I guess the answer to that would be that we would evaluate it. . . .

Q. Would it be fair to conclude that the Postal Service is giving you and your advertisers a good choice with their distribution services?

A. For the total weight that we tend to have in our packages on a weekly basis, that's true.

Q. Okay. Now, from a strictly public policy standpoint, if one of the principal missions of the newspaper industry is to gather news, rather than being in the distribution or alternate delivery business, and one of the missions of the Postal Service is to retain sufficient volume to offer universal service six days a week, doesn't it make sense that the rates for ECR flats and heavier pieces stay attractive enough to retain the business of newspapers?

A. I'm not sure of the question. They're attractive enough now.

Q. So your answer would be yes?

A. I think it would.

(TR19245-19246.)

NAA asserts, "There is precious little evidence that reducing the ECR pound rate would lower advertisers' costs, rather than increasing mailers' profits." (NAA Initial Brief at p.22.) As support for this assertion, NAA quotes SMC Witness Bradpiece's testimony when asked whether he would pass the pound rate reduction onto his customers through reduced preprint rates and he

programs are higher than for full saturation programs. (USPS/AAPS-T1-10(c), Witness White states, "The costs of setting up this type of selective delivery business are quite high." TR19021-19022.)

responded, "It hadn't occurred to me." (TR18963.) This excerpt, and the conclusions drawn from it, are contrary to the context and statements made by Witness Bradpiece in his direct testimony and cross-examination. Bradpiece testified that only 2.5% of the current volumes of his mailed papers were in the pound rate. He stated that the pound rate had, in effect, acted as a cap to the paper's selling efforts. Bradpiece's entire story was that it was "my hope that we would be able to add in more preprints and to produce a heavier product, and so the net result for us from a profit perspective would at least be neutral. . . . As we go out to the box, my postage bill is rising and my revenue isn't." (TR18963.) Bradpiece testified that in the past four years he had not been able to pass on cost increases to his advertisers. He said he supported the USPS ECR proposal and hoped that the increase over 5% in the rate for pieces below 3.3 ounces might be partially offset by a modest reduction in the pound rate. (TR18917-18919.) Bradpiece's entire testimony is hardly support for NAA's assertion that the USPS proposal will only increase mailers' profits.

Most telling on the question of whether or not advertisers will benefit from the USPS ECR proposal is the testimony of Association for Postal Commerce Witness Scott Harding. AAPS and NAA do not even discuss Harding's testimony. Harding, the Chairman and CEO of Newspaper Services of America (NSA), is responsible for buying print media from over 7,800 suppliers including newspapers, TMCs, ADVO, and others. NSA represents large retailers and specialty retailers and is responsible for placing "over 19 billion insertions into newspapers." Harding's interest, "Is that our clients are competitive in the marketplace and improve sales." (PostCom-RT-1 at p.2.) Clearly, Witness Harding thinks the USPS proposals will benefit advertisers. Harding's testimony is compelling evidence of how the USPS proposals will benefit the general public and mailers.

Another example of this selective reading of the record is found in AAPS's Initial Brief at page 10 where it states, "Another fiction that mailers may choose to argue, based upon the

representation of Mr. Baro (TR14389), is that major retailers such as K-Mart and WalMart[sic], specifically identified by Baro, are not likely any longer to be found in shared mail but only newspapers and alternate delivery. Advo's web site proves to the contrary." AAPS's Initial Brief, like its cross-examination, makes much ado of the fact that Advo lists on its web site several national and leading retailers including K-Mart, Wal-Mart, J.C. Penney's, McDonald's, and others. AAPS is accusing AISOP Witness Baro of "fiction," by citing a partial, out-of-context portion of his testimony. Baro, like Witnesses Buckel, Bradpiece, and Giuliano, testified that shared mailers, like the *Miami Flyer*, had difficulty holding on to the business of medium to large size advertisers. Baro stated, "Because of postal rates, the most cost-effective mass media ad program for big stores is usually the media mix that combines TV, radio, and newspapers. Medium and larger advertisers may continue to use our paper in their most productive zones, for new store openings, and seasonal or special sales. . . For national retailers and chain stores, our costs are too high to even be in the running as a mass media choice. You will not find K-Mart, Wal-Mart, or national grocers in our paper." (AISOP-T-2 at p.4 (emphasis supplied).)³ Although Witness Baro was subject to extensive written cross-examination, and appeared in Washington, DC for testimony, neither AAPS nor NAA chose to test his "fictionalized" testimony with cross-examination.

NAA Witness Wilson accused Witness Baro of talking "nonsense" when Baro stated the *Miami Flyer* could not match newspapers' insert rates. Baro stated, "Because our distribution costs are based on postal rates and weight, we cannot cut prices and offer special deals." He described how *The Flyer* could not match some of the prices the *Miami Herald* offered to *The Flyer's* largest

³Witness Giuliano does not maintain that ADVO or other saturation mailers "never" get business of large advertisers. Giuliano explained how postal rates over the last 30 years have caused traditional advertisers with multi-page preprints, weighing more than one ounce, to divert their heavier preprints to nonpostal competitors or reduce the size of their mailed preprints to light weight pieces. (TR18994.)

customers. (TR19227.) Witness Wilson's characterization of Baro's position as "nonsense" was refuted on cross-examination where Wilson admitted that some of the current prices being offered by the *Miami Herald* for a 12-page circular were 3 cents a piece and that the incremental cost for postage alone for a 1.3 ounce circular mailed at the pound rate would be approximately 3.85 cents. (TR19242.) Wilson further admitted that another pricing example he gave in his testimony would require a mailer to pay more than 60% of its revenues to cover the postage costs of an insert. He admitted that it would be difficult for such a mailer to offer an advertiser any further price cuts to match newspaper prices. (TR19230.)

What NAA and AAPS fail to address in their Briefs is the position advanced by AISOP, SMC, PostCom, MOAA, DMA, and the USPS that the USPS's high pound rate has made saturation mail noncompetitive for all but the most light weight advertising of large advertisers and, in many cases, regional and national advertisers are rarely found in coupon envelopes, shared mail packages, shoppers, and free papers. The testimony Witness Buckel gave, that AAPS and NAA ignore, was as follows:

Most saturation mailers depend on a blend of different size customers to survive. Although the mix of advertisers will vary from one saturation mailer to another, most mailers need to maintain some large customers to keep their programs in business. . . . (SMC-T-1 at p.6).

Although individual and small business advertisers are the primary customers we serve, the long term viability of the shared mail industry depends on the extent to which we can compete for retail advertising preprints of the medium to large store customer. . . .

Focusing on the markets with which I am most familiar, the New York and Pittsburgh markets, almost every major retail preprint advertiser has switched from mail delivery to private carrier. . . In major metropolitan areas, where retailers have competitive choices, the major preprint advertisers are not using shared mail services. Daily newspapers, nonpostal TMCs, and private carrier companies are dominating the delivery of retail preprints. . . .

This was my experience at Newport Media. Our lighter papers were customers of the Postal Service. Our biggest paper, and the one carrying the most retail preprints, was

delivered by our own carriers. . . We could deliver our basic paper for 50% of the cost of mail. Additional inserts could be sold into the paper at a very low distribution cost to us and produce significant profits. (SMC-T-1 at pps.10-12.)

AISOP and SMC are not maintaining that saturation mailers never get the business of large advertisers, but have consistently stated that this business is the most vulnerable for them to lose to nonpostal distribution because competitors can offer special deals and cut prices to lure the large customers out of the mail. It is AISOP's position that small businesses suffer, by having a less consumer-attractive product and higher prices to pay, when medium to large advertisers are persuaded to leave shared mail programs. (AISOP-T-2 at p.8; TR18917-18919.)

In concluding the USPS ECR proposals will not help advertisers, NAA and AAPS overlook the testimony of Witnesses Harding and Merriman that advertisers wanting to send heavier pieces, and advertisers and consumers in rural areas, are penalized by the present rate structure that makes heavier pieces so expensive to distribute by mail. Witness Harding states, "The current costing scenario places clients that utilize larger, heavier preprints at a disadvantage as they seek options to most newspaper insertion costs. While most clients may still choose to utilize newspapers as their primary advertising carrier, they find it expensive to supplement the newspaper's distribution shortfall with a mailed product alternative." (PostCom-RT-1 at p.4.) Harding's perspective on the large advertiser's needs is ignored by NAA and AAPS.

Witness Merriman explains how the high pound rate deprives rural consumers of valued shopping information. Merriman explains his paper is the only option for "insert advertisers to reach farm and ranch households in parts of a five-state area. However, these major advertisers are very sensitive to the weight-related prices we must charge. Our plant is constantly getting calls by advertisers wanting to change format, circulation coverage, reducing page count and size, and other inquiries all aimed at allowing them to reduce the weight-related/distribution costs of inserting their ad into our paper. . . The high pound rate results in rural readers getting smaller and lighter flyers

than their cousins in the cities, that provide less shopping information so vital to consumers in our rural market area.” (SMC-T-2 at p.8.) AAPS’s position on Merriman’s testimony and the plight of rural advertisers and consumers is that they should be happy with the status quo. (AAPS Initial Brief at p.3.) There is no evidence that AAPS’s members are providing rural advertisers and consumers with reasonable cost alternate distribution service in these more costly to deliver areas.

NAA, in its Initial Brief, concludes that saturation mailers have not shown that advertisers would benefit by a lower pound rate and states, “What saturation mailers do say is that lowering the pound rate would help them better compete--although they say little how. They overlook the fact that, according to the most recent billing determinants, the mix of ECR mail has already shifted to a greater proportion of pound rated pieces, suggesting that ECR mailers are not having trouble competing at heavier weight mailings.” (NAA Initial Brief at p.23.) Speaking of overlooked facts, NAA fails to mention the testimony of USPS Witness O’Hara where he discusses the same statistical data and points out that the growth of piece and pound related ECR volumes in the high density category has grown while saturation has declined. The ability of newspapers to blend the higher costs of postal delivery with their lower cost carrier force has allowed newspapers to beat shared mailers at their own game. O’Hara states, “From 1998 to 1999, High Density non-letters grew 6.6%, even while Saturation non-letter volume declined 2.4%. The figures for pound rated pieces are even more revealing: High Density grew 17.9%, while Saturation declined 11.1%. These data suggests that saturation mailers are finding less costly alternatives for their heavier pieces. This is troubling--not because it shows a decline in Postal Service volume--but because it shows a decline in volume in a category that is unquestionably overpriced relative to costs.” (USPS-RT-19 at p.6.)

THE (B)(4) BLUFF

In its Initial Brief, AISOP discussed in detail the pretextual nature of Witness Tye’s complaint that the USPS failed to meet its burden for proposing postal rates by not submitting

evidence that showed it considered the effect of its proposals on “enterprises in the private sector of the economy engaged in the delivery of mailed matter other than letters.” This theme is picked up again in NAA’s Initial Brief and is echoed in AAPS’s Initial Brief where it states, “It is disgraceful that the [USPS] witnesses entrusted with considering the impact on competitors and competition as mandated by statute” have not read the SAI studies and have made no inquiries or research on the alternate delivery industry. (AAPS Initial Brief at pps.6-7.) Both AAPS and NAA argue that the USPS has a “high burden” to show in its rate proposals that it considered the effect on enterprises in the private sector.

This argument does not pass the “give me a break” test. Given the history of AAPS and NAA, and their suspicion of the USPS when it comes to ECR rates, can any reasonable person imagine a witness or study that the USPS could offer that NAA and AAPS would consider credible on issues relating to the “effect on competition?” Why should the USPS go through the motions of claiming it has studied the effects on competitors, when the competitors will never believe them?

The Postal Reorganization Act gives the Commission the power to recommend rates and sets forth a variety of criterion for their consideration. If there is a burden to be met in showing the “effect on enterprises in the private sector,” this burden should be met by such enterprises which, unlike the USPS, should be in the best position to obtain and provide this information to the Commission.

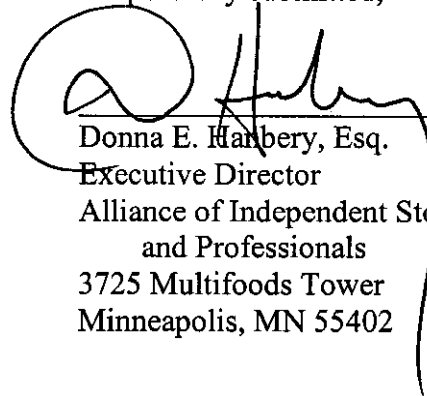
What have the competitors in this case done to submit evidence on their costs, prices, and competitive conditions? Witness Tye presumably had access to, but did not study anything about, the newspaper industry. Indeed, on cross-examination, he showed some confusion in even understanding the difference between saturation deliveries and the selective deliveries that make up newspaper TMC programs. (TR14781; TR14868; TR14996; TR14997.) Likewise, AAPS does not bother to survey or study its membership. Witness White, the sole source of evidence for

competitive harm in this proceeding, did not consider rate or pricing information from other members of AAPS in preparing his testimony or in responding to interrogatories. (MOAA/AAPS-T1-2 and 3; MOAA/AAPS-T1-8 and 9; USPS/AAPS-T1-1 through 5.)

CONCLUSION

The sole claim of competitive harm in this case remains the testimony of Witness White. His testimony is fully rebutted on the record. The Commission has heard evidence from mail associations, individual mailers, large and small advertisers, publishers in major metropolitan areas, where there is competition for the delivery of advertising, and from rural publishers where advertisers and consumers have few choices. The overwhelming weight of evidence in this case favors the recommendation of rates for saturation ECR mail that are no higher than those proposed by the USPS.

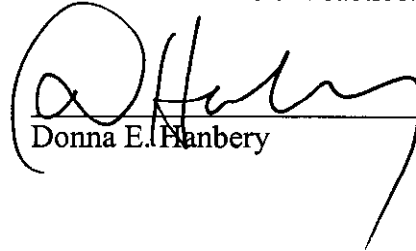
Respectfully submitted,



Donna E. Hanbery, Esq.
Executive Director
Alliance of Independent Store Owners
and Professionals
3725 Multifoods Tower
Minneapolis, MN 55402

CERTIFICATE OF SERVICE

I hereby certify that I have on this date served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.



Donna E. Hanbery

September 22, 2000